

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF OVERLAND DEVELOPMENT,)	
INC. FOR AN ADJUSTMENT OF RATES)	CASE NO.
PURSUANT TO THE ALTERNATIVE RATE)	2007-00204
FILING PROCEDURE FOR SMALL UTILITIES)	

ORDER

On May 23, 2007, Overland Development, Inc (“Overland”) tendered its application requesting the Commission to approve its proposed increase in water rates. Commission Staff, having performed a limited financial review of Overland’s operations, has prepared the attached report containing Staff’s findings and recommendations regarding the proposed rates. All parties should review the report carefully and submit any written comments on Staff’s findings and recommendations or requests for a hearing or informal conference no later than 10 days from the date of this Order.

IT IS THEREFORE ORDERED that:

1. All parties shall, no later than 10 days from the date of this Order, submit written comments, if any, regarding the attached Staff Report or requests for a hearing or informal conference.
2. Any party filing a request for a formal hearing is to include in said request its comments as to the particular finding of the Staff Report to which it objects and a brief summary of testimony it would present at a formal hearing.

3. If no request for a formal hearing or informal conference is received within the 10 days, this case shall stand submitted to the Commission for a decision on all issues raised by the application.

Done at Frankfort, Kentucky, this 11th day of October, 2007.

By the Commission

ATTEST:

A handwritten signature in black ink, consisting of several overlapping loops and a long horizontal stroke at the end, positioned above a horizontal line.

Executive Director

Case No. 2007-00204

STAFF REPORT
ON
OVERLAND DEVELOPMENT INC.
CASE NO. 2007-00204

On May 23, 2007, Overland Development, Inc (“Overland”) tendered its application requesting the Commission approve its proposed increase in its water rates pursuant to Administrative Regulation 807 KAR 5:076. Overland provided a billing analysis of its test-period water sales showing that its proposed water rates will generate annual revenues of \$47,338,¹ which is \$8,809 or 22.86 percent over normalized test period revenues from water sales of \$38,529.² Using its billing analysis, Staff determined that Overland’s requested rates actually produce annual revenues of \$51,658, which is \$10,704 or 26.14 percent over Staff’s normalized revenues of \$40,954.

In order to evaluate the requested increase Commission Staff performed a limited financial review of Overland’s test period operations for the 2006 calendar year. The Scope of Staff’s review was limited to obtaining information as to whether the test period operating revenues and expenses were representative of normal operations. Insignificant of immaterial discrepancies were not pursued and are not addressed herein.

¹ Application, Usage Table, Revenue from Present Rates.

² Id., Usage Table, Revenue from Present Rates.

Mark Frost and Lisa Taylor of the Commission's Division of Financial Analysis performed the limited review on August 15, 2007. This report summarizes Staff's review and recommendations. Mr. Frost is responsible for the preparation of this Staff Report except for the determination of normalized operating revenue and Appendix C, Staffs recommended rates, which were prepared by Jason Green.

Overland did not include a pro forma income statement in its Application. In Exhibit A of the Application, Overland calculates expense increases of \$8,827, as shown in Table 1 below:

Table 1: Overland's Proposed Expense Increases	
Salary Increase	\$ 7,200
Purchased Water	837
Sample Tests	130
Postage	142
PSC Property tax	+ 518
Total	\$ 8,827

Based upon Staff's recommendations, Overland's operating statement would appear as set forth in Appendix A. The revenue requirement determination, Appendix B of Staff's Report, shows that Overland's pro forma operations support a revenue requirement from water rates of \$39,802, a decrease in revenues of \$1,152. The rates contained in Appendix C produce Staff's recommended revenue requirement.

Signatures

Prepared by: Mark C. Frost
 Financial Analyst, Water and Sewer
 Revenue Requirements Branch
 Division of Financial Analysis

Prepared by: Jason Green
 Rate Analyst, Water and Sewer Rate
 Design Branch
 Division of Financial Analysis

APPENDIX A
STAFF REPORT CASE NO. 2007-00204
PRO FORMA INCOME STATEMENT

	<u>Test-Period Operations</u>	<u>Pro Forma Adjustments</u>	<u>Adj. Ref</u>	<u>Pro Forma Operations</u>
Operating Revenues:				
Metered Water Sales	\$ 37,278	\$ 3,676	(a)	\$ 40,954
Operating Expenses:				
Operation & Maintenance:				
Salaries & Wages - Owners	\$ 12,000	\$ 0		\$ 12,000
Purchased Water	12,897	2,707	(b)	15,604
Contractual Services	785	60	(c)	845
Water Testing/Analysis	375	0		375
Telephone	1,242	(428)	(d)	814
PSC Assessment	65	0		65
Postage	515	99	(e)	614
Accounting Fees	1,500	0		1,500
Training/License	362	0		362
Penalties	7	0		7
Backhoe - Fuel & Oil	30	0		30
Backhoe - Repair	840	0		840
Total Operation & Maint. Exp	<u>\$ 30,618</u>	<u>\$ 2,438</u>		<u>\$ 33,056</u>
Depreciation	1,956	(1,956)	(f)	0
Amortization	0	0		0
Taxes Other Than Income:				
Payroll Taxes	1,064	0		1,064
Other Tax & License	1,155	(1,155)	(a)	0
Income Tax Expense	363	(363)	(g)	0
Utility Operating Expenses	<u>\$ 35,156</u>	<u>\$ (1,036)</u>		<u>\$ 34,120</u>
Utility Operating Income	<u>\$ 2,122</u>	<u>\$ 4,712</u>		<u>\$ 6,834</u>
Other Income & Deductions:				
Interest Income	20	0		20
Net Income Available for Debt Service	<u><u>\$ 2,142</u></u>	<u><u>\$ 4,712</u></u>		<u><u>\$ 6,854</u></u>

a. Metered Water Sales. In its 2006 Annual Report,³ Overland reported test-period revenues from metered water sales of \$37,278. Attached to the Application is a test period billing analysis, wherein Overland calculates normalized revenues of \$38,592 based upon water sales of 5,416,000 gallons.

Overland provided Staff with its test-period customer billing records in a Microsoft Excel spreadsheet. Using this information, Staff determined that the test-period water sales were actually 5,957,000 gallons, 551,000 gallons above the amount Overland reported. Overland attributed the 551,000 gallon difference to free service given to Jim Taylor, Overland’s owner and sole shareholder, and to customer billing adjustments. Overland admitted that it did not maintain adequate records to support the customer billing adjustments and that its adjustment policy is not included in the tariff.

In calculating its normalized revenues, Overland used rates different than those contained in the tariff. Overland explained that it had grossed-up the tariffed rates to include the county school tax. Also, Overland has reported the county school tax of \$1,155 as an operating expense. In Table 2 below is the comparison of the rates in the application to the tariffed rates:

	<u>Rate Block</u>		<u>Application</u>	<u>Tariff</u>	<u>Differences</u>
First	2,000	Min. Bill	\$ 16.82	\$ 16.32	3.06%
Next	8,000	Gallons	\$ 6.04	\$ 5.86	3.07%
Next	20,000	Gallons	\$ 4.49	\$ 4.36	2.98%
Next	20,000	Gallons	\$ 3.68	\$ 3.57	3.08%
Over	50,000	Gallons	\$ 2.90	\$ 2.81	3.20%

³ Annual Report of Overland to the Public Service Commission of the Commonwealth of Kentucky for the Calendar Year Ended December 31, 2006 (“2006 Annual Report”) at 24.

Overland is acting as an agent of the taxing authorities to collect and remit school taxes. Accordingly, these monies should not be reported by Overland as either an operating revenue or expense. For this reason Staff is not including the school tax in its calculation of pro forma revenues and is recommending that operating expenses be reduced by \$1,155 to remove the school taxes from operating expenses.

Using the unadjusted water sales of 5,957,000 gallons and the current tariffed rates, Staff calculates normalized operating revenues from retail water sales of \$40,954, \$3,676 above the amount reported in Overland's 2006 Annual Report. Staff recommends the Commission increase operating revenues by \$3,676 to reflect the results of its billing analysis.

b. Purchased Water. Overland proposes to increase test-period purchased water expense of \$12,725 by \$837 for a pro forma level of \$13,652. Since Overland's last purchased water adjustment in 2003 there have been two wholesale water rate increases. Applying the estimate of the difference in the wholesale rate of \$0.12 per 1,000 gallons to the reported test-period purchases of 6,979,000 gallons, Overland calculates a purchased water adjustment of \$837.

Although Overland reports purchasing 6,979,000 gallons of water in its 2006 Annual Report, Staff's review of the invoices from the Big Sandy Water District ("Big Sandy") shows that they actually purchased 7,243,700 gallons. In the letter dated March 2, 2007, Big Sandy informed Overland that effective April 1, 2007 the wholesale water rate would increase from \$0.96 to \$1.25 per 1,000 gallons.

By multiplying test period purchases of 7,243,700 gallons by the April 1, 2007 wholesale water rate and including the monthly minimum bill of \$545.75, Staff calculates

a pro forma purchased water expense of \$15,604.⁴ Accordingly, Overland’s adjustment should be denied and purchased water expense increased by \$2,707 to reflect Staff’s pro forma level of \$15,604.

c. Contractual Services. Overland reports test-period contractual services expense of \$785, inclusive of meter reading fees of \$720. Currently Overland is paying its meter reader a fee of \$65 per month or \$780 annually.⁵ Staff recommends that contractual services be increased by \$60 to reflect the annual cost of \$780.

d. Telephone. Overland’s test-period telephone expense of \$1,242 includes \$856, the cost of Mr. Taylor’s cellular telephone. Staff notes that Mr. Taylor has other business interests besides Overland. Staff believes that the cellular telephone is not used solely for the benefit of Overland, and therefore, 100 percent of the cellular telephone cost should not be borne by Overland’s ratepayers. Allocating 50 percent of the test-period cellular telephone expense to the other businesses results in a decrease to the test-period telephone expense of \$428.

e. Postage. Overland reports a test-period postage expense of \$515. Using the current postage rate of \$0.41, the number of bills in Staff’s billing analysis, and the monthly UPS fee of \$8 for mailing the effluent test results, Staff calculates a pro forma

⁴ \$545.75 (Minimum Bill) x 12 (Months) = 7,243.70 (Gallons) x \$1.25 (Rate per 1,000 Gal.) = Pro Forma Purchased Water Expense	\$ 6,549 + 9,055 <u>\$ 15,604</u>
⁵ \$65 (Monthly Fee) x 12 (Months) =	<u>\$ 780</u>

postage expense of \$614.⁶ Staff recommends that postage expense be increased by \$99 to reflect its pro forma level.

f. Depreciation. Overland reports a test-period depreciation expense of \$1,956. In reviewing Overland's depreciation schedule, Staff notes that all of the assets listed were either fully depreciated at the end of the calendar year 2006 or will be fully depreciated at the end of calendar year 2007. Given, that the current depreciation will not be an on-going expense after 2007, Staff proposes to eliminate the depreciation expense of \$1,956 from Overland's pro forma operations.

g. Income Tax. Overland reports a test period income tax expense of \$363. Staff is recommending that test-period operations be reduced by \$365 because the allowance for this expense is included in its revenue gross-up calculation.

⁶ 1,264 (Bills) x \$0.41 (Postage Rate) =	\$ 518
\$8 (UPS charge) x 12 (No. of Tests) =	+ 96
Pro Forma Postage	<u>\$ 614</u>

APPENDIX B
STAFF REPORT CASE NO. 2007-00204
REVENUE REQUIREMENT DETERMINATION

<u>Revenue Requirement</u>	
Operating Expenses	\$ 34,120
Divided by: Operating Ratio	÷ 88%
Revenue Requirement before Income Tax Gross-up	<u>\$ 38,773</u>
Less: Operating Expenses	- 34,120
Net Income After Income Taxes	<u>\$ 4,653</u>
Multiplied by: Income Tax Gross-up	x 1.2254902
Net Income Before Income Tax	<u>\$ 5,702</u>
Add: Operating Expenses	+ 34,120
Revenue Requirement before Interest Exp.	<u>\$ 39,822</u>
Less: Interest Income	- 20
Revenue Requirement - Sewer Rates	<u>\$ 39,802</u>
Less: Normalized Operating Revenue	- 40,954
Recommended Revenue Decrease	<u><u>\$ (1,152)</u></u>

APPENDIX C
STAFF REPORT CASE NO. 2007-00204
STAFF'S RECOMMENDED WATER RATES

RATES AND CHARGES

First	2,000	gallons	\$ 15.86	Minimum bill
Next	8,000	gallons	\$ 5.70	per 1,000 gallons
Next	20,000	gallons	\$ 4.24	per 1,000 gallons
Next	20,000	gallons	\$ 3.47	per 1,000 gallons
Over	50,000	gallons	\$ 2.73	per 1,000 gallons